DOCUMENT RESUME

ED 158 330 CS 204 332

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TITLE Pay Cable: A Viable Advertising Medium?
PUB DATE Aug 78
NOTE 12p.; Paper presented at the Annual Meeting of the Association for Education in Journalism (61st, Seattle, Washington, August 13-16, 1978)

EDRS PRICE MF-$0.83 HC-$1.67 Plus Postage.
DESCRIPTORS Broadcast Industry; Broadcast Television; *Cable Television; *Community Antennas; Federal Court Litigation; *Marketing; Mass Media; *Television Commercials
IDENTIFIERS *Advertising; *Pay Cable Television

ABSTRACT

Cable television, which cannot only clarify local signals to weak signal areas but can also bring in distant signals to areas which have been receiving few signals, has the capacity to present special television programs to customers for extra fees. The number of pay cable subscribers is growing and industry projections are that it will reach 20 million by 1980. A United States Appeals Court recently overthrew a Federal Communications Commission rule which had banned advertising on the pay cable channels. This court ruling opened a large potential market for advertisers. Some factors limiting the attractiveness of pay cable advertising are: (1) although cable television has grown over the years, the disconnect rate is high and this might keep the industry from permitting advertisements since a strong selling point has been "no commercial interruptions," (2) it is not clear that the industry projection of 20 million users by 1980 is accurate, and (3) there is little current penetration of pay cable in the large urban areas. (TJ)

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PAY CABLE: A VIABLE ADVERTISING MEDIUM?

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Presented to the Advertising Division, Association for Education in Journalism Annual Convention, Seattle, Washington, August 1978.

CS204332

PAY CABLE: A Viable Advertising Medium?

Introduction

The intention of this paper is to examine some of the issues surrounding the potential use of pay cable as an advertising medium. While the cable industry has always been allowed to sell advertising over its local origination channels, it has not, until recently, been allowed to advertise over its premium program pay channels for which subscribers are charged an additional cost. Prior to 1977 the FCC did not allow advertising over the pay channels. However, a recent decision by the Court of Appeals (D.C. Circuit) overruled the FCC restraints (1).

Some advertising industry sources have stated that pay cable subscribers will number 20,000,000 by 1980 and that the Court's recent ruling will open up a new medium for advertisers (2, 3). In light of the recent ruling and advertising industry speculation, it is now appropriate to assess the potential for utilizing pay cable as an advertising medium.

Cable Development

Cable television was one of the first technologies that offered a realistic bypass to the "bottleneck" created by the limited off-the-air broadcast spectrum. Cable allowed home television reception via coaxial cable rather than the traditional off-the-air signals. Television dealers developed the concept of coaxial cable distribution as a means for selling television sets. The first such systems in the late 1940s used a larger master antenna to bring clarity to otherwise poor signals and a coaxial cable to carry this signal to individual homes. This antenna-cable system provided a better picture and, therefore, gave individuals a reason to purchase television sets.

Lansford, Pennsylvania, appears to have been the first commercial venture in community antenna television. Because Lansford is 65 miles from Philadelphia and overshadowed by mountains, the Philadelphia signals Lansford received were understandably weak. In 1949 Robert L. Tarlton set up a master antenna on a mountain near Lansford and began amplifying the signals to full strength and sending them down the mountain on coaxial cables directly into individual homes. Tarlton charged a $125 installation charge fee and a $3 monthly service charge (4).

In 1950, 70 communities had cable systems, and approximately 14,000 homes were being served. By 1976, 3,700 cable systems served 12.5 million homes in approximately 8,000 communities (5). The 12.5 million homes represented 16 percent of the total television homes. Although the main purpose of the early cable systems was to clarify signals, the subsequent growth in cable systems was due to their use in areas that had limited or no television service.

While the Federal Communications Commission has an established policy of advocating local over-the-air broadcast stations, it is very difficult to operate a profitable television broadcasting operation in the 1,200 communities outside the top 100 markets. Station hardware, production, and talent fees were and still are generally too high compared to the revenues generated by advertising in small communities (6). The potential television audiences in these areas are too small to warrant large amounts of advertising, and since broadcasters depend on advertising for most of their revenues, it is difficult for the small stations to remain profitable.

Such a situation is ripe for the cable operator, since cable cannot only clarify local signals but bring in distant signals to areas that have been receiving few if any off-the-air signals. Moreover, cable is a local business

in that businesspersons in the area help set up the cable systems and make them more acceptable to the community (6).

Cable systems are inherently different from over-the-air broadcasters. Broadcasters are very much concerned with production, program origination, and advertising revenues, while most cable operators are initially concerned with the re-transmission of already existing off-the-air signals and subscriber rates. Because it emphasizes re-transmissions, cable is not tied to the costs of program production or the advertising revenue structure. It can thus operate on different premises that allow it to serve areas local broadcast stations cannot. In 1977 the typical cable installation fee was $15 and the average monthly charge $6.25 (6).

However, the potential of cable technology proved far greater than the mere amplification of signals:

> When a current of signal is introduced into a cable, an electromagnetic interaction takes place between the center wire and the surrounding sheath. This is the secret of the cable's key characteristic — its immense capacity for carrying electronic signals, data, and information. One of cable TV's greatest potentials is its inherent ability to end this (over-the-air electromagnetic spectrum) economy of scale (4).

At the very minimum, cable stations can carry twelve channels. Many can carry upward of twenty, and systems with a potential capacity of 40 channels are common. Using this channel capacity, the local cable operator can do more than merely clarify weak signals. By utilizing microwave and even satellite technology, a cable operator can bring distant signals into the community.

Cable's ability to introduce a vast amount of new signals applies not only to the re-transmission of programming from over-the-air broadcasters. Cable television operators can originate their own programming or obtain programming from other sources. Many cable operators currently are originating their own programming in one form or another. Programs such as local sports, city council

meetings, and local news are being produced and distributed by cable operators. Some cable operators set aside one or more channels to offer mechanical sources such as stock market ticker tapes, news wire services, and/or time and temperature (7).

Pay Cable

Some cable operators have taken an approach to programming called pay cable. This involved the cable system purchasing programming from independent distributors (see Table 1). The cable system then sells this premium programming to its subscribers. The programming is usually on a designated cable channel for which subscribers pay an additional monthly rate. This programming usually "includes current movies, sports programming not available on commercial TV, drama, cultural, children's programs, and entertainment specials" (5).

The typical pay cable fee is $7.87 over and above the regular cable subscription fee (8). Currently, 1,000,000 cable subscribers are purchasing some form of pay cable. Projections indicate this will have increased by 14 to 16 percent in 1977. As noted earlier, one industry source speculates this will climb to 20,000,000 by 1980 (2).

Pay Cable, the FCC, and the Courts

An important consideration at this juncture is the U.S. Appeals Court decision regarding the FCC pay cable rules (1). Previously, FCC rules limited the types of programming that could be sold over the pay cable channels. The FCC rule was primarily promulgated to avoid pay cable sources from taking away (siphoning-off) programming from over-the-air broadcasters. In part, the FCC argument rested with the concept that if programs were siphoned-off to pay channels, poor people would not be afforded the opportunity to see the previously

TABLE 1

PAY-CABLE DISTRIBUTOR/BOOKERS WITH MARKET SHARES

Distributor	# Systems Booked	# Subscribers	% Share of Pay-Cable Market
Home Box Office	234	585,981	59.9%
TeleMation Program Services	40	207,705	21.2
Self-booked systems	23	62,618	6.4
Optical Systems Ch. 100	15	44,308	4.5
SHOWTIME	10	25,213	2.6
Hollywood Home Theatre	4	17,493	1.8
Pay TV Services	10	17,364	1.7
BestVision	23	9,733	1.0
Cinemerica	5	7,394	0.7
	364	977,809	100.0%

"free" programming. Additionally, the FCC rules prohibited the selling of advertising on the pay cable channels.

The U.S. Court of Appeals overturned the FCC pay cable rules. Basically, the Court noted that broadcaster allegations that pay cable would siphon-off broadcaster programming fare was unsupported. While the Court pointed out that the FCC's "siphoning-off" argument was conjectural, it also noted that the anti-advertising rule was: (1) not well thought out, and (2) perhaps inconsistent with the FCC argument concerning the poor.

> Equally important, the pay cable rules taken as a whole scarcely demonstrate a consistent solicitude for the poor. Thus, although "free" home viewing relies upon advertiser-supported programming, the Commission has in this proceeding barred cable firms from offering advertising in connection with subscription operations. See note 55 supra. As a result, the Commission forecloses the possibility that some combination of user fees and advertising might make subscription cable television available to the poor, giving them access to the diverse programming cable may potentially bring. As has already been noted, see pages 46-48 supra, the advertising ban section of the regulations was developed to meet wholly different regulatory problems and it has been retained here, not because of its intrinsic merit, but only because no one objected too much. We are thus left with the conclusion that, if the Commission is serious about helping the poor, its regulations are arbitrary; but if it is serious about its rules, it cannot really be relying on harm to the poor. Whatever may be the ultimate validity of this argument, its principal defect on this review is that there is no record evidence to support it (1, p. 59).

Pay Cable Advertising

As noted, approximately 1 million cable subscribers are currently purchasing pay cable. While the previously stated projection of 20,000,000 pay TV subscribers may be a blue-sky estimate, some potential growth does exist.

Although the 1 million current cable subscribers who also purchase pay cable represent less than 8 percent of all cable subscribers, it is important to note that they represent 22 percent of all cable subscribers who are on a cable system that offers pay cable (see Table 2).

TABLE 2

OVERALL INDUSTRY FIGURES INCLUDING: CABLE SYSTEMS AND SUBSCRIBERS, CABLE SYSTEMS OFFERING PAY, AND PAY CABLE SUBSCRIBERS

Total Cable Systems	8,000
Total Cable Subscribers	12,500,000
Cable Systems Offering Pay Cable	364
Number of Basic Cable Subscribers of Systems Offering Pay Cable	4,369,575
Pay Cable Subscribers	977,809

Pay cable subscribers total 8 percent of all cable subscribers and 22 percent of cable subscribers who are linked to cable systems offering a pay service.

As shown in Table 2, the 364 cable systems which offer pay cable reach 4.37 million people or approximately one-third of the total cable industry (8). Therefore, the 22 percent pay cable penetration becomes important because large cable systems are now offering pay cable. If cable growth continues and eventually penetrates a majority of the metropolitan areas, pay cable would then appear to have a large chance of succeeding. In view of the U.S. Appeals Court ruling, allowing advertising over pay cable, the advertising industry may have a new television source in which to air commercials.

Some Limiting Factors

Even though the courts have at least temporarily allowed pay cable advertising, it does not necessarily follow that pro-cable sources will be anxious to air commercials. The National Cable Television Association (NCTA) and pay cable sources such as Home Box Office, a subsidiary of Time, Inc., have been promoting pay cable programming as free from commercial interference (3, 5).

While pay cable has grown over the years, there has been some problem with the high disconnect rate among users. Industry sources note the disconnect rates are approaching 25 percent in some markets and have even reached 100 percent in a few markets. While new subscribers are adopting the pay service, many do not stay with the service (9).

Although some of this high disconnect rate is due to population movement, other factors are said to be involved. In part, this high disconnect rate has been blamed on pay cable systems placing their good programming early in the schedule; "This inevitably led to a disappointment on the part of the viewer and a resultant disconnect" (9, p. 16).

This acknowledged industry problem leads one to wonder if the pay cable sources (Table 1) are willing to show advertisements over their systems, which originally promised no commercial interruption. At this juncture, no evidence has been cited to indicate if consumers are willing to accept commercial interruptions, provided there would be a subsequent reduction of monthly pay cable subscription cost.

Another obstacle in the development of pay cable advertising is the penetration of cable and pay cable. While Table 2 indicates cable has currently penetrated 12.5 million homes and pay cable approximately 1 million, there has been a slow movement in the more urban markets. While cable penetration estimates have suggested that it will be available to 50-60 percent of the U.S. homes by 1981, there can be no guarantee that figure will eventuate (10). Without cable penetration in the more urban areas, and eventual pay cable adoption in these areas, the concept of pay cable advertising may not become an integral factor in the advertising industry.

Discussion

Due to recent court rulings, the advertising industry is legally allowed to use pay cable channels in order to disseminate commercial messages. At first glance this appears to be a worthwhile opportunity because of the select groups viewing and the potential growth of the pay cable industry.

However, industry predictions that pay cable will eventuate to 20,000,000 subscribers, on a system that is partially supported by advertising, may be overzealous. There are still too many unanswered questions involved ranging from further court rulings, pay cable industry acceptance, consumer acceptance, and eventual pay cable growth.

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